

May 6, 2016

Reference Number: 16-0010

Monica A. Crusse, Chairperson
Office of Minority Business Enterprise
Maryland Department of Transportation
7201 Corporate Center Drive
Hanover, Maryland 21076

Dear Ms. Crusse:

By letter dated October 1, 2015, AutoFlex, Inc. (AutoFlex) appeals the Maryland Department of Transportation's (MDOT's) denial of its application for expanded certification as a Disadvantaged Business Enterprise (DBE) in certain requested NAICS codes under criteria set forth at 49 C.F.R. Part 26 (the Regulation).

In the Denial Letter (Denial Letter) dated September 14, 2015, MDOT cites the following grounds¹ for denying certification:

- 1) Failure to meet the requirements of §26.71(b): The disadvantaged owner's firm is dependent on the expertise and resources of another nondisadvantaged firm;
- 2) Failure to meet the requirements of §26.71(g): The disadvantaged owner does not have the overall understanding as well as technical competence and experience directly related to, the firm's operations and the type of work in the NAICS codes it is applying for;
- 3) Failure to meet the requirements of §26.71(n): The disadvantaged owner does not control the firm in the additional types of work within the requested NAICS codes;
- 4) The applicant firm is affiliated with a nondisadvantaged firm due to identity of interest, shared equipment, and other resources under 13 CFR §121.103; and
- 5) There are concerns regarding the size standard and number of employees with regard to 13 CFR §121.106.²

¹ The certifier did not explain its would-be denial rationales under §26.71(b); §121.101(a); §121.103; and §121.106 with the specificity that §26.86(a) requires.

² MDOT did not determine whether the firm satisfies the size standard because it lacked information concerning the number of employees at the nondisadvantaged venture.

We have carefully considered the full administrative record. We remand to MDOT to reconsider the determination of ineligibility as to whether the disadvantaged owner has an overall understanding of, and managerial and technical competence and expertise directly related to, the wholesale operations described in the requested NAICS codes, within the meaning of §§26.71(g) and (n). The firm need only establish that it is more likely than not that the owner controls the firm with respect to the wholesaler NAICS codes. See generally §26.61(b) (preponderance of the evidence standard). If MDOT finds that the disadvantaged owner does satisfy the requirements for these provisions, it should certify the firm. If not, MDOT must produce a new Denial Letter fully addressing its concerns pursuant to §§26.71(g) and (n) in further consideration and clarification of evidence in the Record.

Applicable Regulation Provisions

§26.61(b) provides:

“The firm seeking certification has the burden of demonstrating to you, by a preponderance of the evidence, that it meets the requirements of this subpart concerning group membership or individual disadvantage, business size, ownership, and control.” (Emphasis added.)

§26.71(b) provides:

“Only an independent business may be certified as a DBE. An independent business is one the viability of which does not depend on its relationship with another firm or firms.

(1) In determining whether a potential DBE is an independent business, you must scrutinize relationships with non-DBE firms, in such areas as personnel, facilities, equipment, financial and/or bonding support, and other resources.

(2) You must consider whether present or recent employer/employee relationships between the disadvantaged owner(s) of the potential DBE and non-DBE firms or persons associated with non-DBE firms compromise the independence of the potential DBE firm.

(3) You must examine the firm's relationships with prime contractors to determine whether a pattern of exclusive or primary dealings with a prime contractor compromises the independence of the potential DBE firm.

(4) In considering factors related to the independence of a potential DBE firm, you must consider the consistency of relationships between the potential DBE and non-DBE firms with normal industry practice.”

§26.71(g) provides:

“The socially and economically disadvantaged owners must have an overall understanding of, and managerial and technical competence and experience directly related to, the type of business in which the firm is engaged and the firm's operations. The socially and economically disadvantaged owners are not required to have experience or expertise in every critical area of

the firm's operations, or to have greater experience or expertise in a given field than managers or key employees. *The socially and economically disadvantaged owners must have the ability to intelligently and critically evaluate information presented by other participants in the firm's activities and to use this information to make independent decisions concerning the firm's daily operations, management, and policymaking.* Generally, expertise limited to office management, administration, or bookkeeping functions unrelated to the principal business activities of the firm is insufficient to demonstrate control.” (Emphasis added.)

§26.71(n) states in pertinent part:

“You must grant certification to a firm only for specific types of work in which the socially and economically disadvantaged owners have the ability to control the firm. To become certified in an additional type of work, the firm need demonstrate to you only that its socially and economically disadvantaged owners are able to control the firm with respect to that type of work. You must not require that the firm be recertified or submit a new application for certification, but you must verify the disadvantaged owner's control of the firm in the additional type of work.”

§26.86(a) provides:

“When you deny a request by a firm, which is not currently certified with you, to be certified as a DBE, you must provide the firm a written explanation of the reasons for the denial, specifically referencing the evidence in the record that supports each reason for the denial. All documents and other information on which the denial is based must be made available to the applicant, on request.”

13 CFR §121.101(a) provides:

“SBA's size standards define whether a business entity is small and, thus, eligible for Government programs and preferences reserved for “small business” concerns. Size standards have been established for types of economic activity, or industry, generally under the North American Industry Classification System (NAICS).”

13 CFR §121.103(a) provides:

“(1) Concerns and entities are affiliates of each other when one controls or has the power to control the other, or a third party or parties controls or has the power to control both. It does not matter whether control is exercised, so long as the power to control exists.

(2) SBA considers factors such as ownership, management, previous relationships with or ties to another concern, and contractual relationships, in determining whether affiliation exists.

(3) Control may be affirmative or negative. Negative control includes, but is not limited to, instances where a minority shareholder has the ability, under the concern's charter, by-laws, or shareholder's agreement, to prevent a quorum or otherwise block action by the board of directors or shareholders.

(4) Affiliation may be found where an individual, concern, or entity exercises control indirectly through a third party.

(5) In determining whether affiliation exists, SBA will consider the totality of the circumstances, and may find affiliation even though no single factor is sufficient to constitute affiliation.

(6) In determining the concern's size, SBA counts the receipts, employees, or other measure of size of the concern whose size is at issue and all of its domestic and foreign affiliates, regardless of whether the affiliates are organized for profit.

(7) For SBA's Small Business Innovation Research (SBIR) and Small Business Technology Transfer (STTR) programs, the bases for affiliation are set forth in § 121.702."

13 CFR §121.106(b) in pertinent part provides:

"Where the size standard is number of employees, the method for determining a concern's size includes the following principles:

(1) The average number of employees of the concern is used (including the employees of its domestic and foreign affiliates) based upon numbers of employees for each of the pay periods for the preceding completed 12 calendar months.

(2) Part-time and temporary employees are counted the same as full-time employees.

(3) If a concern has not been in business for 12 months, the average number of employees is used for each of the pay periods during which it has been in business.

(4)(i) The average number of employees of a business concern with affiliates is calculated by adding the average number of employees of the business concern with the average number of employees of each affiliate. If a concern has acquired an affiliate or been acquired as an affiliate during the applicable period of measurement or before the date on which it self-certified as small, the employees counted in determining size status include the employees of the acquired or acquiring concern. Furthermore, this aggregation applies for the entire period of measurement, not just the period after the affiliation arose."

§26.86(a) provides:

"When you deny a request by a firm, which is not currently certified with you, to be certified as a DBE, you must provide the firm a written explanation of the reasons for the denial, specifically referencing the evidence in the record that supports each reason for the denial. All documents and other information on which the denial is based must be made available to the applicant, on request."

§26.89(f)(1) provides:

“The Department affirms [the certifier’s] decision unless it determines, based on the entire administrative record, that [the] decision is unsupported by substantial evidence or inconsistent with the substantive or procedural provisions of this part concerning certification.”

§26.89(g) provides:

“All decisions under this section are administratively final, and are not subject to petitions for reconsideration.”

Operative Facts

Louis D. McDonald is the owner of AutoFlex (Expansion of Services Investigative Report (Report) dated May 29, 2015 at 1). The firm was established on January 14, 1987. Id. at 2. Mr. MacDonald is the President and owns 100% of the firm. Id. Mr. McDonald is of Hispanic descent. Id.

The Report and résumé indicate that AutoFlex is a commercial vehicle leasing company providing vehicles for fleets that deliver specialty food products and meats. The firm is currently leasing refrigerated delivery trucks to Harvest Foods Group, a meat manufacturer. Id. at 5.

Due to Mr. MacDonald’s government contract experience, Harvest Foods Group approached Mr. MacDonald to enter into agreement with them. Id. at 6. The two parties executed a Distributor Agreement titled Manufacturer’s Certificate of Appointment (Certificate) on November 11, 2014. Id. The Certificate indicates that AutoFlex is an appointed Distributor, authorized to resell and enter into Federal, State Government and Commercial Contracts in order to supply and deliver USDA certified specialty meat products under NAICS codes **424470** wholesale and **424420** packaged meats.

The Denial Letter indicates that AutoFlex applied with MDOT for expansion of services in the following areas:

424410-General Line Grocery Merchant Wholesalers;
424420-Packaged Frozen Food Merchant Wholesalers;
424470-Merchant and Meat Product Merchant Wholesalers; and
425120-Wholesale Trade Agents and Brokers.

The firm has been certified in **425120-Wholesale Trade Agents and Brokers.** Id. MDOT did not grant AutoFlex’s request with respect to the other codes. Id. at 2. MDOT denied Mr. MacDonald’s request for expansion due to his lack of expertise and experience within the requested codes, “You [Mr. MacDonald] have no direct experience in the wholesale distribution of meat and other food products. It is Harvest Foods who have the experience and expertise in the wholesale distribution of meat products.” Id. at 3.

Mr. MacDonald’s résumé indicates the following with regard to his food wholesaler industry experience: he worked for Marriott Hotel Management as the Catering Food Services Manager in 1980; entered into a Distributor Agreement with Harvest Foods Group; and is the Founder and

President of AutoFlex, Inc. from 1987 to the present. Mr. MacDonald also studied Restaurant Management in Food & Nutrition from Colorado State University from 1978 to 1980. Id.

Mr. MacDonald describes the distribution process and his firm's role in the agreement with Harvest Foods Group in the Report. Harvest Foods Group will slaughter the animal, and the carcass will be shipped through refrigerated trucks leased from AutoFlex to the state prison for cutting and packaging. Id. at 6. Afterward, AutoFlex will pick up the meet products and deliver to clients or Government Agencies. Id.

The Maryland Minority Business Enterprise Advisory Committee (MBEAC) Hearing dated June 17, 2015, indicates:

“...I’ve got 20—more than 20 years experience with the food industry in providing transportation vehicles, refrigerated box trucks, that type of thing...I mean, we’ve leased the refrigerated boxes that go to Camp David for the [p]resident... Id. at 8.

Mr. MacDonald has experience dealing with Department of Defense and Army and Army commissaries. Id. He further states:

“I’ve been certified by MDOT since 1989 as a fleet management and leasing company. I manage fleets. I lease fleets.” Id. at 10.

“I also have the approved NAICS codes to provide infrastructure, right, for alternative fuel vehicles.” Id.

...
“...I know the [food] industry. I studied it in school. I worked at Marriot Corporation which is headquartered here in Maryland and I know about how to buy meat, how to sell meat, you know, how to be involved with that industry.

So, it’s [wholesaler industry] a natural progression. It’s [wholesaler industry] a natural expansion of services, and we’re hoping to gain your [MDOT’s] support.” Id. at 9-11.

...
“What we are asking for is the [certification within the requested] NAICS codes so that we can now go to the government, right Federal, State et cetera, and represent ourselves as having the capabilities to supply the meats to them. And so we would deliver supply—we would be the supplier, an authorized supplier, as a distributor of the manufacturer. The meat plant is basically a manufacturer, okay, and we in essence are the distributor.” Id. at 14.

...
“...they [Harvest Foods Group] appointed me as the distributor so that I’m authorized to sell... I am an added distributor and I have the ability to do government contracts.” Id. at 17-18.

With regard as to whether Mr. MacDonald qualifies as a “wholesaler,” he states:

“In essence, I am the contractor, okay? I am the contractor to the State [of Maryland] and to the Federal agency that’s interested in buying the meat. If the State National Guard puts out a request for quote, I will respond to it. I will have all the pricing put together and packaged. I will submit the proposal which I prepare, based on what the pricing of the meats are for that day or for that week, et cetera. Right?

And it’s no different than leasing a vehicle from me, okay? I am packaging a proposal, submitting it to the agency interested in that product or commodity, or you know, meat right? And if they [government entities/clients] accept my proposal and they like the pricing that we provide, and then they do a best value of, okay, I’m buying it from the Midwest from a large company, or I’ll buy from a local small business in Maryland.” Id. at 18-19.

Mr. MacDonald indicates that his definition of “distributor” is “reseller.” Id. at 26.

Discussion and Decision

We find no substantial evidence in the record to support the proposition that AutoFlex and Harvest Foods Group are “affiliates,” within the meaning of the SBA regulations quoted above. *See generally* §26.65. Therefore, we view the question as being simply whether AutoFlex has met its burden of proof under Regulation §26.71.

Section §26.71(n) sets forth the rule concerning requests for expansion of the work areas in which a DBE firm is certified. A recipient, under §26.71(n) “must grant certification to a firm only for specific types of work in which the socially and economically disadvantaged owners have the ability to control the firm.” The issue in this case is whether the firm has demonstrated that its disadvantaged owner has sufficient understanding, expertise, and experience to control the firm in its requested work areas. Specifically, under §26.71(g), AutoFlex has the burden of demonstrating, by a preponderance of the evidence, that Mr. MacDonald has an overall understanding of the relevant work areas which is sufficient to make informed, critical, and independent decisions regarding operations within each NAICS code (**424410-** General Line Grocery merchant Wholesalers; **424420-** Packaged Frozen Food Merchant Wholesalers; and **424470-** Merchant and Meat Product Merchant Wholesalers).

NAICS codes

We find that the denial of expansion in the requested NAICS codes needs further clarification as there is evidence in the Record to substantiate Mr. MacDonald’s knowledge and control of the wholesaler industry. The denial letter does not specifically address the individual NAICS codes. It simply states, in apparent error, that Mr. MacDonald has *no experience* in the requested work areas.

The Record indicates that AutoFlex picks up the meat packages from Harvest Foods Group. AutoFlex then delivers the meat to the State Prison for cutting and packaging. Afterward, AutoFlex picks the meat products up and distributes or resells the meat to government entities. These appear to be classic transportation, distribution, and resale activities, as evidenced, e.g., by

the distribution agreement. Mr. MacDonald has extensive experience transporting and handling food products. He has also dealt with government entities. He was educated in the food business. To obtain NAICS codes in the wholesaling industry would arguably be a natural progression of AutoFlex's services. The aforementioned facts may satisfy the requirements of §§26.71(g) and (n).

In the Denial Letter, MDOT indicates that Harvest Foods Group has the required technical experience required for the business. However, the distribution agreement specifies that AutoFlex's role is different from Harvest Food Group's. AutoFlex, under the agreement, performs the distribution and resale activities. Section 26.71(g), further, does not require the disadvantaged owner to have necessarily greater technical experience than other participants in the business; that section, instead, requires an "overall understanding" sufficient to make informed, critical business decisions. Mr. MacDonald makes a point that wholesaling meat is not much different than his other current services. He creates pricing packages based on meat products instead of leased vehicles, and presents the packages to government clients. Harvest Foods Group also appointed AutoFlex as a contractor or reseller to government clients. We remand for MDOT to reconsider the determination and the evidence in the Record.

Conclusion

We remand under §26.89(f)(4) and direct MDOT to reconsider the ineligibility determination due to evidence in the Record as to whether Mr. MacDonald has an overall understanding and managerial and technical competence and experience related to the requested NAICS codes per §§26.71(g) and (n).

If MDOT finds that Mr. MacDonald satisfies the requirements of these provisions, MDOT should certify. If not, MDOT must produce a new Denial Letter specifying its concerns under these provisions and citing specific supporting evidence in the Record.

This decision is administratively final and is not subject to petitions for reconsideration.

Sincerely,

Samuel F. Brooks
DBE Appeal Team Lead
External Civil Rights Programs Division

cc: AutoFlex, Inc.